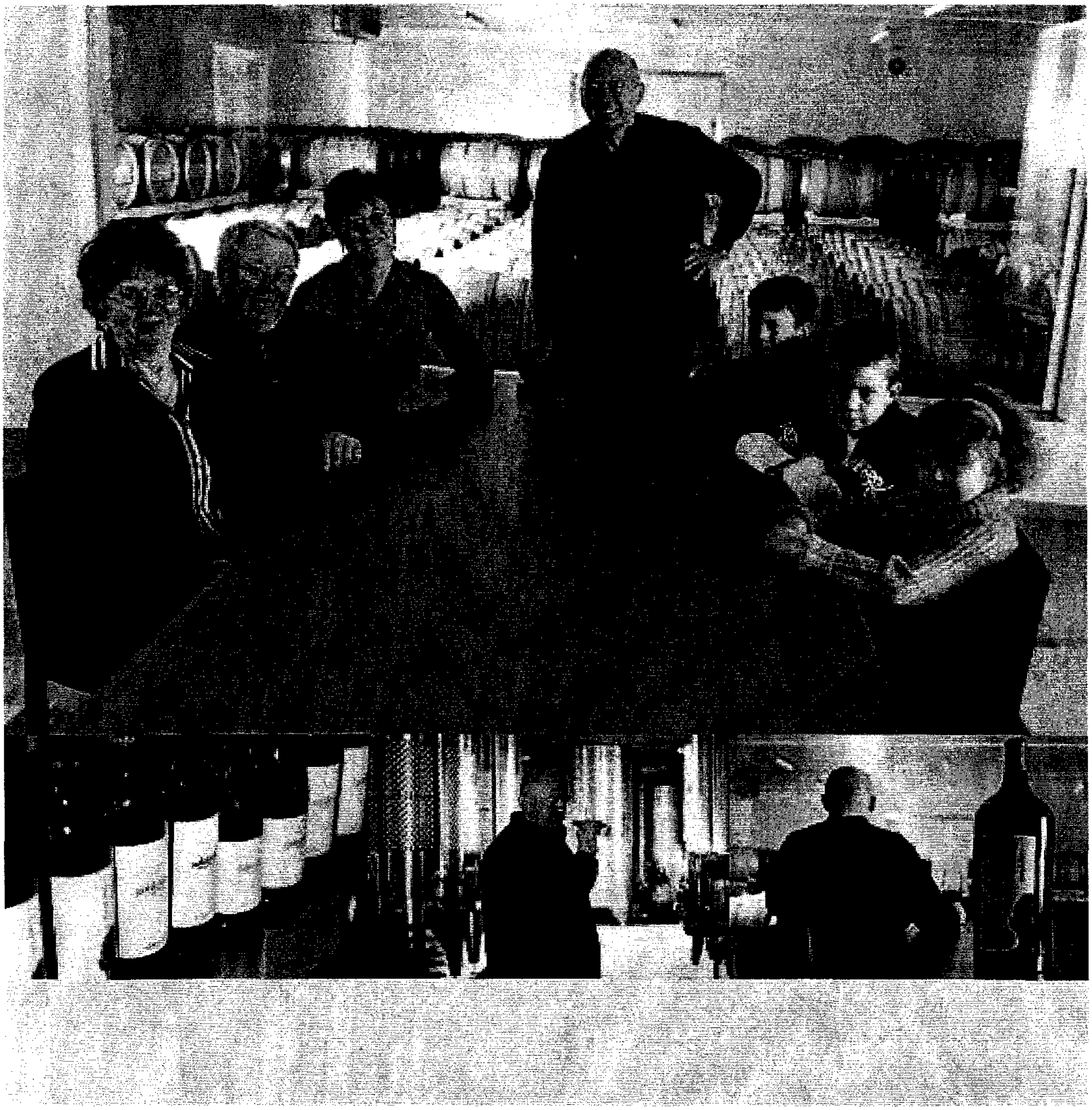
Goldenits family, clients of Erste Bank, Austria



AUSTRIA

The Austria segment includes most banking activities in Austria and additional activities conducted on a group-wide basis. It is divided into four sub-segments: Savings Banks, Retail and Mortgage, Large Corporates, and Trading and Investment Banking.

ECONOMIC REVIEW

Our Austrian businesses operated against a stable economic background in 2005. The Austrian economy outperformed Eurozone growth for the fourth year running, and continued on its path of stable growth. Real GDP rose by 1.7% in 2005, while GDP/capita hit a level of EUR 29,800, among the highest in the European Union. Exports and domestic demand contributed in equal measure to overall growth. In 2005 exports accounted for some 52% of GDP. The unemployment rate deteriorated somewhat to 5.0%, but remained well below the Eurozone average of 8.5%.

The inflationary environment remained benign with consumer price inflation edging up only slightly to 2.2%. As this was the trend throughout the Eurozone, short term interest rates were flat at 2.1%. In December 2005 the European Central Bank has for the first time in more than five years raised interest rates and indicated that further rises may be on the horizon, following an improved growth outlook for Eurozone countries.

Austria's external position as represented by the current account balance continued to stay in positive territory, helped along by a strong trade balance: it amounted to 0.8% of GDP as opposed to 0.3% in 2004. The general government balance deteriorated significantly in 2005 to -1.9%, triggered by higher public spending, but remained well inside the limits set out by the Stability and Growth Pact.

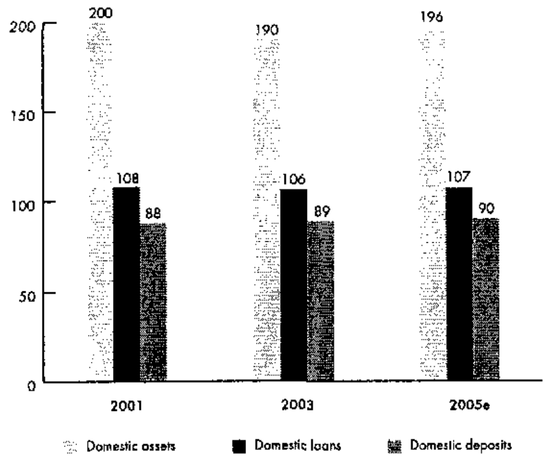
MARKET REVIEW

Austria's domestic banking market shows all the features of a mature western market: a high degree of competitive tension, high operating costs and low profit margins; and a market structure that is not conducive to operating at above average levels of profitability due to the high number of non-shareholder oriented institutions. Despite this scenario the Austrian market offers selected growth opportunities in such areas as mortgages and wealth management.

Key economic indicators – Austria	2002	2003	2004	2005e
Population (ave, million)	8.1	8.1	8.2	8.2
GDP (nominal, EUR billion)	220.7	227.0	237.0	245.0
GDP/capita (in EUR thousand)	27.3	28.0	29.0	29.8
GDP growth (real, in %)	1.0	1.4	2.4	1.7
o/w: domestic demand contribution (in %)	-0.7	2.5	0.7	0.9
Exports (% of GDP)	48.7	48.4	51.0	51.9
Imports (% of GDP)	43.9	44.8	46.1	46.7
Unemployment (% of labour force)	4.2	4.3	4.8	5.0
Consumer price inflation (ave, in %)	1.7	1.3	2.0	2.2
Interest rate (1m interbank offer rate, in %)	3.3	2.3	2.1	2.1
EUR FX rate (ave)	1.0	1.0	1.0	1.0
EUR FX rate (eop)	1.0	1.0	1.0	1.0
Current account balance (% of GDP)	0.3	-0.5	0.3	0.8
General government balance (% of GDP)	-0.4	-1.2	-1.0	-1.9

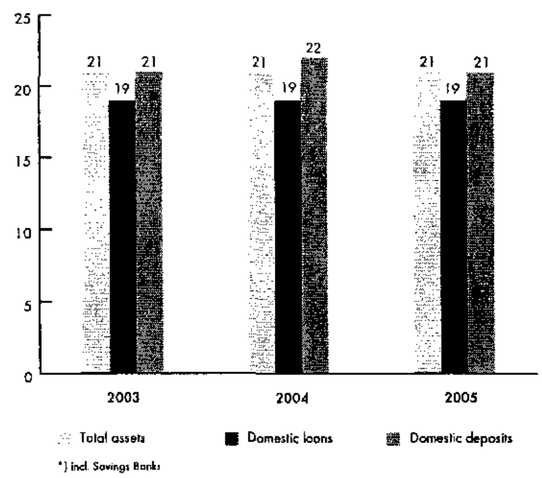
Source: Eurostat.

Financial intermediation – Austria (in % of GDP)



Source: Oesterreichische Nationalbank, Eurostat.

Erste Bank market shares – Austria*) (in %)



Source: Erste Bank, Oesterreichische Nationalbank.

Overall market aggregates, i.e. those including foreign assets, also paint a very positive picture, reflecting the Austrian banks' push into Central and Eastern Europe. In 2005 total banking assets/GDP were just shy of 300%, an impressive level even by international standards and up from 272% in 2001. Growth in the Austrian market is lopsided, though. While the total market grows strongly on the back of the ever increasing central and east European exposure, the domestic asset/GDP ratio has been hovering around the 190% mark for the past decade, or so. A similar dichotomy can be observed for such other aggregates as deposits and loans. Domestic aggregates grow in line with GDP, while foreign aggregates tend to grow in excess of both Austrian and local GDP.

In unison with the stable development of the domestic market, Erste Bank maintained its position as one of the leading Austrian banks. In 2005 it intermittently edged its nearest competitor to the No. 1 spot with a 21% total asset market share. In addition, Erste Bank held similar market shares in domestic deposits and loans. It served some 2.8 million customers through a network of some 987 own and savings bank branches as well as electronic channels.

SAVINGS BANKS/HAFTUNGSVERBUND

Business profile. In 2005 the Savings Banks segment encompassed 45 Austrian savings banks that were consolidated as a result of their membership in the Haftungsverbund and in which Erste Bank AG held little or no equity interest. Savings banks that are majority-owned by Erste Bank AG (Salzburger Sparkasse, Tiroler Sparkasse and Sparkasse Hainburg-Bruck-Neusiedl) are included in the Retail and Mortgage segment.

The relationship between Erste Bank AG and the savings banks is to the mutual benefit of both parties. Erste Bank AG provides a wide range of services and products to the savings banks and its customers. These services and products include syndication, asset management and securities-related services, risk management and legal advice, as well as retail mortgage, life insurance and investment fund products, which enable independent savings banks to reduce costs while providing full service to their clients. In return Erste Bank AG has access to a large additional distribution network of some 711 branches for its products without the operational costs associated with operating of additional branches.

In addition Erste Bank AG and the savings banks cooperate on such key operational issues, as common product development; the projection of a unified identity through a one-brand strategy; the standardisation of business and marketing strategies for retail and corporate banking; the development of common management information and control systems and integration of central functions; and the introduction of a common performance-related remuneration scheme for management.

BUSINESS REVIEW

Strategy. The Savings Bank segment continues to focus on strengthening its existing strong ties to Erste Bank AG. This co-operation is intended to bolster the distribution and market development capabilities while promoting an efficient division of labour within the organisation, up-to-date human resources policies and appropriate decision-making structures. Other key goals include optimising customer service while improving profitability.

Successful market presence. In 2005, Erste Bank AG and the savings banks were once again able to expand their client share in Austria. The overall client share increased to 27.7%, while main client share increased to 22.6%. As in previous years, Erste Bank and the savings banks once again received top honours in advertising recognition across all banking sectors.

Greater efficiency through modern IT. In 2005, several technological improvements were implemented that resulted directly in greater efficiency. A more targeted customer relationship management software coupled with the necessary employee training led to better sales results. "s Abwicklungsmanagement" will provide the Lending and Securities divisions with electronic document management software. The "Business Intelligence" project will create a common database for compliance with Basle II requirements and the soon to be established risk-oriented reporting system. Finally, the Internet portal of the savings banks has been totally updated. These projects are all illustrative of the major projects in 2005.

Common risk management policy. As part of the development of a common risk management policy, the savings banks successfully implemented or started joint projects on Basle II, credit business minimum standards and risk-oriented reporting.

Outlook

In 2006, the savings banks intend to step up their combined efforts in sales and cross-selling. Moreover, they will focus on themes such as retirement savings, real estate, bank cards and structured products. They will also focus on implementing best practices management techniques and increase the use of benchmarking.

This year, the savings banks also plan to generate further cost-saving synergies in the area of development and processing costs and improve their market success through the upgraded customer relationship management programmes.

Financial review

in EUR million	2005	2004
Pre-tax profit	185.2	182.1
Net profit after taxes and minority interests	3.2	7.1
Cost/income ratio in %	68.1	67.5
Return on equity in %	1.3	2.9

Net profit after taxes and minority interests contracted by EUR 3.9 million from EUR 7.1 million to EUR 3.2 million. Return on equity fell from 2.9% to 1.3%, while the cost/income ratio increased slightly from 67.5% to 68.1%.

As expected, net interest income declined by 1.8%, or EUR 15.5 million, from EUR 849.6 million to EUR 834.0 million. This decrease resulted from persistent low interest rates and a highly competitive market environment. Risk provisions were up sharply from the previous year, increasing by EUR 31.2 million from EUR 184.5 million to EUR 215.8 million. The increase followed two one-off negative events at two of the savings banks. Given the relatively insignificant equity interest in these banks, net profit after taxes and minority interests was only marginally affected.

Net commission income trended very favourably, rising by 12.3%, or EUR 39.4 million. This gain was generated primarily in the funds business as well as through securities sales commissions. It reflects the successful co-operation between Erste Bank and the savings banks.

General administrative expenses increased by 3.0%, or EUR 23.9 million, from EUR 801.7 million to EUR 825.6 million. At a rate of 3.0% this growth outpaced inflation only slightly. The other operating result improved by EUR 32.6 million, from a loss of EUR 18.8 million in 2004 to a gain of EUR 13.8 million last year, despite non-recurring gains in 2004 from the sale of a Haftungsverbund savings bank's branches and thanks to financial asset valuation gains.

RETAIL AND MORTGAGE

Business profile. The Retail and Mortgage segment comprises all activities in Austria relating to retail, mortgage and small and medium-sized corporate customers. More specifically, it includes Erste Bank's 142 strong own branch network in eastern Austria, including Vienna, which predominantly serves professionals, retail clients and SMEs. As noted above, it also includes three majority-owned savings banks (Salzburger Sparkasse, Tiroler Sparkasse, Sparkasse Hainburg-Bruck-Neusiedl).

A portion of the results of the investment fund business (Erste-Sparinvest), consisting of private banking and portfolio management for retail customers, and of the life insurance business (s Versicherung), are also included in this sub-segment. Erste-Sparinvest is the market leader in retail funds in Austria and No. 2 overall, while s Versicherung, which is the exclusive partner to Erste Bank, the savings banks and s Bausparkasse, leads the Austrian life insurance market.

Furthermore Erste Bank's Austrian retail real estate and mortgage activities form part of this segment, covering retail mortgages, non-profit, subsidised and commercial housing finance, and property management and brokerage. The main operating units are building society s Bausparkasse – market leader in Austria – which finances private and non-profit housing development and is also responsible for Erste Bank´s mortgage bond transactions as of 2005; property agency s REAL, with 84 offices across Austria; and s Wohnbaubank, a specialist property finance provider.

BUSINESS REVIEW

Strategy. While the Retail and Mortgage segment comprises a diverse range of financial services businesses the common denominator is the strategic focus on the retail customer. Collectively, Erste Bank aims to offer its retail customers a one stop solution for all their financing and investment needs, irrespective of the distribution channel they use. The same holds true for retail mortgages and related services as well as for commercial and publicly subsidised property financing. Within this framework Erste Bank aims to adapt to the quickly changing regulatory environment for subsidised residential property development and building society saving plans.

Highlights 2005

Own branches outperform targets. The performance of Erste Bank's own branch network was excellent in 2005. On the back of a strong domestic stock market and increasing public awareness for private old age provision, securities commissions rose by 24%, while securities based savings plans leapt ahead by 62%. The strong demand for retail mortgages equally contributed to the strong showing of Erste Bank's own branch network, as did high sales volumes for government-subsidised and private pension products.

SME business achieves turnaround in 2005. Following years of unsatisfactory business performance, our SME business has successfully completed its restructuring efforts in 2005 and made a positive contribution to group profit. The business unit expanded operating profit by 45% to EUR 26.5 million, while keeping volumes stable. This progress was mainly due to higher commission income and tight cost management. An improved portfolio composition led to a decrease in risk provisions. Overall, these developments translated into a net profit of EUR 4.5 million and substantial uplift in the cost/income ratio and return on equity. This performance was achieved despite ongoing, difficult market conditions and thanks successful cross-selling into the existing client base.

Solid gains in the mortgage business. In 2005 we expanded our housing finance volumes both through Erste Bank AG and s Bausparkasse. Total loan volume increased from EUR 10.3 billion to EUR 11.2 billion. 2005 also brought a regulatory change for subsidised building society savings: which can now also be used

to finance education and care home expenses. In response Erste Bank developed and successfully marketed a number of new tailor-made products.

Rapid growth in fund management. Erste-Sparinvest continued to grow faster than the market in 2005. The firm's performance was also recognised by such fund rating agencies as Standard & Poor's, Morningstar, Lipper and Feri Rating & Research. According to Morningstar, Erste-Sparinvest ranked No. 1 among 36 European bond funds. Operationally, Erste-Sparinvest extended its market share to 18.0%. Funds under management grew to EUR 28.1 billion by year-end 2005, up from EUR 21.5 billion a year earlier, helping comfortably maintain its position as the second largest fund manager in Austria. In retail funds Erste Bank's fund management unit maintained its market leadership.

Life insurance growth continues apace. s Versicherung further expanded its market leadership position in Austrian life insurance in 2005, reaching a market share of about 15.3%, up on last year's 14.3%. In total the portfolio of policies, covering life and accident policies, exceeded the one million mark in 2005 for the first time ever. Correspondingly, gross premium written lept from EUR 900 million in 2004 to EUR 1.1 billion in 2005. s Versicherung also successfully expanded its position in the market for government-incentivised retirement savings products.

Outlook 2006

Through the businesses that are consolidated into the Retail and Mortgage segment we will continue to exploit the growth opportunities that do exist in the Austrian market: these are essentially centred on wealth management and wealth creation. Private old age provision, be in the form of recurring savings plans, investment funds, private or government subsidised pension plans, and multi-purpose building society savings will remain top sales priorities for us. Residential mortgages will also be a key growth driver. In the area of commercial and non-profit housing finance the focus will be student and care homes. In financial terms the segment targets a return on equity of 11% in 2006, after having more than doubled this metric in 2005 to 10%.

Financial review

in EUR million	2005	2004
Pre-tax profit	151.6	76.3
Net profit after taxes and minority interests	93.2	41.1
Cost/income ratio in %	72.2	76.0
Return on equity in %	10.1	5.0

In 2005, the Retail and Mortgage segment, including the savings banks in which Erste Bank AG holds a majority interest, performed very satisfactorily. Net profit after taxes and minority interests more than doubled, rising by EUR 52.2 million from EUR 41.1 million to EUR 93.2 million, while the return on equity in this segment exceeded the 10% target level for the first time and the cost/income ratio contracted sharply from 76.0% to 72.2%.

As expected, net interest income contracted by 1.0%, or EUR 5.0 million. This decrease occurred mainly in the branch network as a result of persistent low interest rates. Meanwhile, s Bausparkasse, which is also assigned to this segment, recorded strong gains thanks to the expiration of high-rate deposits. Loan loss provision expense trended favourably, falling by 11.6%, or EUR 13.8 million from EUR 118.9 million to EUR 105.1 million. This decrease resulted mainly from the improved risk situation in the SME business as well as at Tiroler Sparkasse.

Net commission income, which increased by 11.6%, or EUR 34.1 million, from EUR 280.4 million to EUR 314.5 million, made a substantial earnings contribution to this segment. This increase was driven by noticeable gains in the securities business — in the branch network and at the Tirol and Salzburg savings banks — as well as through Erste-Sparinvest's improved earnings in the retail funds business. The SME business also contributed through an increase in the number of real estate lease agreements and guarantees.

General administrative expenses were reduced by 1.7%, or EUR 10.7 million, through a strict cost control policy in the branch network and SME business. The other operating result improved from a loss of EUR 5.5 million to a gain of EUR 16.2 million, mainly through proceeds on disposals and project-related income.

LARGE CORPORATES

Business profile. The Large Corporates segment caters to domestic and international corporate customers with sales of EUR 70 million and above and sovereign borrowers. Following the establishment of the business unit Group Large Corporates within this segment and as part of the New Group Architecture efficiency programme in January 2005, the Large Corporate segment now acts as a one stop shop for corporate customers across Central and Eastern Europe: it offers project finance for commercial real estate in Austria and abroad, other forms of structured finance, trade finance, debt and equity corporate finance services, export financing as well as documentary credits and guarantees, in addition to general commercial lending.

A small component of the investment fund business, institutional clients, is also included in the Large Corporates segment. Furthermore, Immorent, Erste Bank's leasing specialist for real estate and equipment, also forms part of the Large Corporates segment. Immorent is a full-service provider of complete solutions in leasing, real estate-related services and real estate investment products. In line with Erste Bank's regional strategy, Immorent has also expanded its activities into Central and Eastern Europe and currently has subsidiaries in the Czech Republic, Slovakia, Hungary, Slovenia, Croatia, Serbia, Bulgaria and Romania.

BUSINESS REVIEW

Strategy. The Large Corporates segment seeks to cover the entire value chain proactively, comprehensively and across borders through tailored customer care. To further deepen our client relationships and to reflect the growing importance of the central and east European markets we have established the Group Large Corporates business unit as of 2005. As a result a group-wide client relationship manager has been assigned to each large corporate client with annual sales in excess of EUR 175 million. The relationship manager serves all the client's needs by tapping the resources of country and product teams, thereby providing a single source of advice. A primary strategic goal of this measure is cross-border market share growth in investment banking, especially in corporate finance. To this effect, we are particularly focused on arranging more debt and equity transactions in Central and Eastern Europe.

Highlights 2005

Improved market position in corporate finance. Our corporate finance business performed well in 2005, driven mainly by the continued expansion of our clients' activities in Central and Eastern Europe. Last year, corporate bond financing was especially popular, given the favourable interest rates and declining risk premiums across all risk classes. Erste Bank also recorded outstanding performances in equity financing. We had lead roles in the equity offerings by Wiener Städtische Versicherung (deal size: EUR 1,050 million) and by s Immo AG (deal size: EUR 267 million).

Strong growth in financing of real estate funds. Although the development of new real estate development projects in Central and Eastern Europe remained flat at a high level, the investment activities of Austrian and foreign real estate funds continued apace. These investments led to several transactions, in particular the financing of the Airport Logistic Park in Prague, the financing of a portfolio of shopping centers in Hungary and of a real estate portfolio in Poland.

Tourism financing on solid ground. Last year, tourism properties were increasingly prized by international investors and financial institutions as investments and finance projects. In a competitive environment, Erste Bank successfully increased its financing volume. Its acquisition financing on behalf of Walton Street Capital for the Prague Marriott Hotel, including the Millennium Plaza office and commercial centre, achieved international recognition.

Outlook 2006

The successful establishment of the "Group Large Corporates" department will also have a favourable impact in 2006 and is expected to lead to a further strengthening of the risk-return ratio, despite an unfavourable lending business environment marked by unsatisfactory margins. The growing focus on fee and project financing businesses to complement the traditional lending business is also expected to yield positive results. Finally, we expect capital market transactions to increase significantly in both number and volume, given the above-average growth in Central and Eastern Europe. This growth applies to both equity and debt financing.

Financial review

in EUR million	2005	2004
Pre-tax profit	77.8	83.8
Net profit after taxes and minority interests	55.5	55.8
Cost/income ratio in %	39.4	39.1
Return on equity in %	11.0	12.6

Last year, the operating result of the Large Corporates segment increased by 6.1% from EUR 129.3 million to EUR 137.2 million. Business volume increased slightly by 3.1%, or EUR 530 million, with the growth concentrated mainly in the area of lease financing. Net interest income increased by 2.2%, or EUR 3.0 million, from EUR 139.9 million to EUR 142.9 million.

Net commission income advanced significantly by 15.4%, or EUR 11.0 million, from EUR 71.2 million to EUR 82.2 million. Commissions on capital market and leasing transactions contributed to this positive development.

The other operating result contracted by EUR 21.3 million from a loss of EUR 7.7 million to a loss of EUR 29.0 million. Last year, the volume of project-related provisions, reflected in the other operating result, was essentially unchanged from 2004. Risk provision allocations declined by 19.6% from EUR 37.9 million to EUR 30.5 million, as the decline in provision allocations for the financing business was only partially offset by a modest increase in provision allocations in the leasing business.

General administrative expenses increased by 7.7% from EUR 83.0 million to EUR 89.4 million, mainly as a result of the leasing business' growth in the extended home market (legal and advisory) and through the establishment of new processes.

In the Large Corporates segment, net profit after taxes and minority interests remained essentially unchanged. Given the generally higher equity allocation, the return on equity dipped slightly to 11.0% and the cost/income ratio was 39.4%. The very favourable earnings trend in net interest income and net commission income was offset by the higher costs and expenses in the other operating result.

TRADING AND INVESTMENT BANKING

Business profile. The Trading and Investment Banking segment comprises third-party and proprietary trading activities in Vienna, London, New York and Hong Kong, as well as asset-liability management. Amongst others the segment carris out the following tasks on behalf of the group:

- **_Management of asset-liability risk (interest rate and liquidity risks) for Erste Bank Group**
- **_Foreign currency, fixed-income and securities trading products for all client groups**
- **_Development of structured products, especially for all central and east European growth markets**

The aforementioned establishment of the Group Large Corporates business unit in 2005 led to a reallocation of the investment banking functions, such that large corporate clients are now served by a single entity. Capital market transactions are therefore processed by the Group Large Corporates unit, while the traditional equities business (trading, sales) has been integrated into the Group Treasury business unit. This change created synergies in the trading business and a pooling of resources for the structuring of investment and financing products.

BUSINESS REVIEW

Strategy. The Trading and Investment Banking segment's strategic goal is to be the best product provider in Central and Eastern Europe. We want to provide optimum service for our retail and institutional clients in their investment activities. Product innovation is also essential. By continuously developing and extending our product range, we enable our clients to participate directly in the future success of the central and east European growth markets. For trading, we leverage our market position as one of the region's largest liquidity providers as well as our market knowledge and proximity.

Highlights 2005

Expansion of our equities market position and launch of the New Europe Blue Chip Index (NTX). Last year, Erste Bank again further expanded its market position in central and east European securities trading. Relative to total trading volume

on the local stock exchanges, our market share in 2005 was as follows:

2005	Market share	Average Market position
Erste Bank (Vienna)	19.57%	2
Erste Bank Investment Hungary	19.10%	1
Česká spořitelna	9.01%	3
Slovenská sporiteľňa	2.26%	10
Erste Securities Polska	3.75%	9
Erste Securities Zagreb	7.71%	4

Source: Local stock exchanges.

The creation of the New Europe Blue Chip Index (NTX) as a new benchmark for the central and east European growth markets is noteworthy. The NTX includes the 30 largest and most liquid stocks in the region, and was launched jointly with the Vienna Stock Exchange in autumn 2005. In the fourth quarter of 2005 alone, we placed EUR 165 million in index-based products such as investment funds, certificates and warrants.

After having steadily built-up our equity derivatives product range, we added two further distribution channels in this area last year. We created our own Internet portal, which can be accessed at www.erstebank-derivate.at. In addition, Erste Bank is now present as an issuer on EUWAX, Europe's largest derivatives exchange.

First CDO placement in Central and Eastern Europe. Erste Bank extended its credit market leadership in Central and Eastern Europe through the development of a new product. Last year, working with an international partner, we capitalised on our expertise and ongoing technology investments by successfully placing a collateralised debt obligation in our core markets.

Treasury products for large corporates and SMEs. In 2005, we satisfied the ever-growing demand from our corporate clients for hedging foreign currency, interest rate and liquidity risk. On the interest rate and currency side, Erste Bank developed more than 50 new structured products that enable our large corporate clients and SMEs to implement innovative zero-cost strategies. Last year, income from this product group more than doubled. We expect similar growth in the years ahead.

Outlook 2006

In 2006, the focus of the Trading and Investment Banking segment will again be on innovative structured products. We would like to expand our product range by adding new asset classes such as commodities. The goal is not only to increase volume, but also the level of in-house production. By expanding our product range and working closely with the savings banks, our medium-sized enterprise clients will benefit from currency and interest rate hedging and optimisation. For our institutional clients, meanwhile, we remain a key partner for their equities trading in Central and Eastern Europe. Furthermore, our competency in the central and east European markets will also play a growing role in the credit area and lead to innovative products. Along with credit trading, we want to offer our clients assets and liabilities management advisory services in 2006.

Financial review

in EUR million	2005	2004
Pre-tax profit	122.2	140.8
Net profit after taxes and minority interests	90.3	105.6
Cost/income ratio in %	43.3	38.8
Return on equity in %	31.9	43.2

Net profit after taxes and minority interests contracted by 14.4%, or EUR 15.2 million from EUR 105.6 million to EUR 90.3 million, as the very favourable trend in net commission income did not fully offset the market-led decline in net interest income. The return on equity fell from 43.2% to 31.9%, while the cost/income ratio increased from 38.8% to 43.3%.

The segment result breaks down differently from the previous year. The asset-liability management result fell by around EUR 40 million, mainly as a result of interest rate trends and currency hedging effects, while earnings in the Treasury segment increased by 33%, or EUR 25 million.

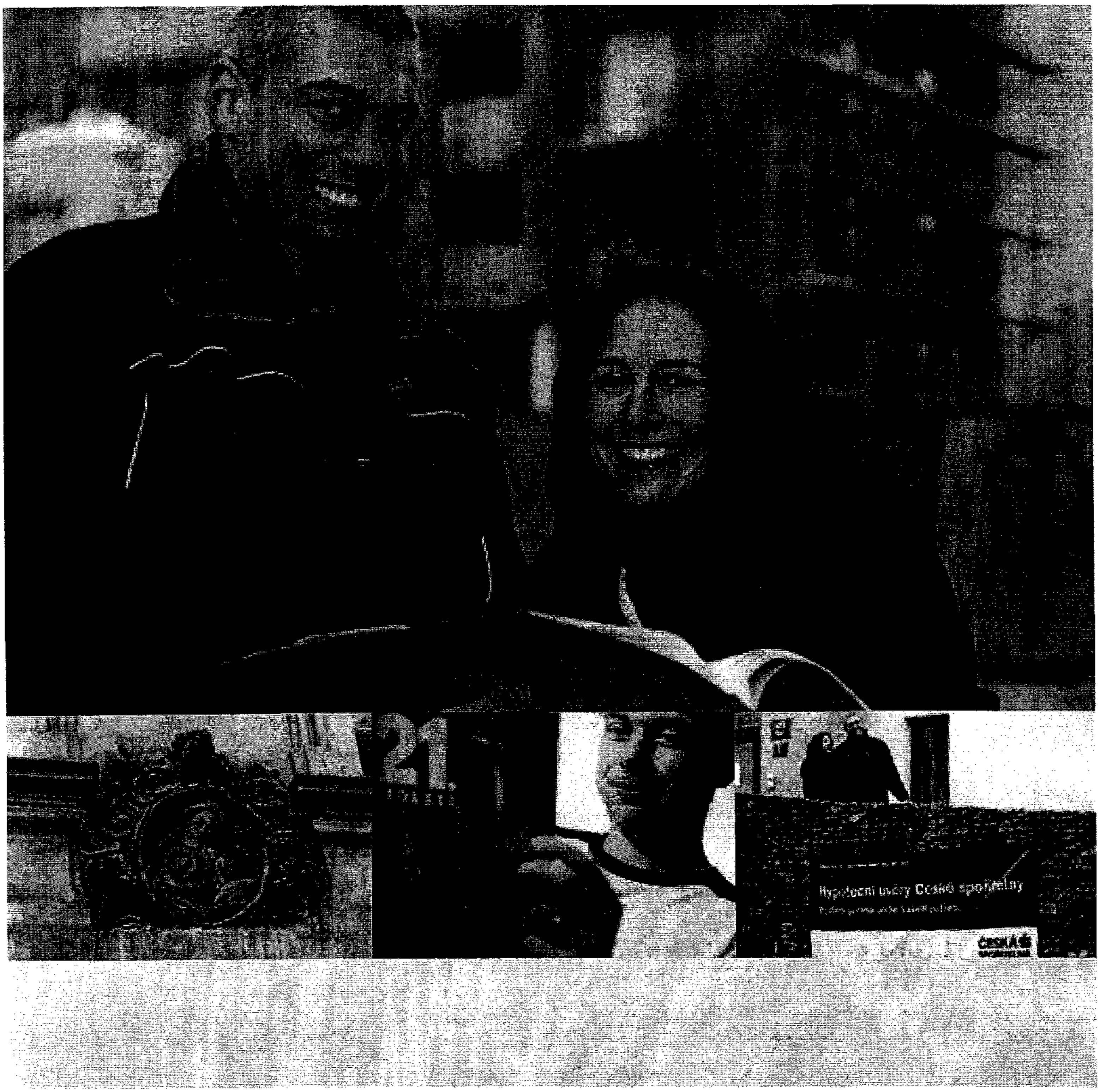
The expected decline in net interest income by 39.3%, or EUR 40.3 million, from EUR 102.4 million to EUR 62.2 million was due to low interest rate levels, a flat yield curve and the impact of currency hedging on the results of our central European subsidiaries.

"For now we have bought the apartment"

Barbora Jarosova and her husband, Jiri Jaros, live and work in Prague, the capital of the Czech Republic. Barbora is an events manager for a large events agency, while Jiri is responsible for data processing at a bank. They are both contributing to their country's tremendous economic resurgence. Since the fall of the Iron Curtain, the Czech Republic has become one of the most successful economies of all the former Eastern Bloc countries. With 5% GDP growth and per capita GDP of EUR 9,600, the Czech Republic leads the way not only among the new EU members but throughout all of Central and Eastern Europe. Thus it comes as no surprise that in the centre of all this activity, Prague is brimming with optimism as well as business and construction activity. Many residents are taking advantage of this situation. The Jarosovas are among them, and have purchased a modern apartment under construction in a Prague suburb.

Erste Bank: "Ms Jarosova and Mr Jaros, when will your new apartment be finished?"
Jiri Jaros: "Very soon! In May or June, we can move into the new building. Of course, we have a nice home now, since it all depends on what you make of it, right? But naturally we are looking forward to the new building."
Barbora Jarosova: "It will be different. The new apartment is more than 60 square metres larger than our current one, and everything is new: the building and fixtures. It's an exciting time."
Jiri Jaros: "One should not forget that we are paying a lot of money for it. Nowadays, the cost of living in Prague is as high as in many west European capitals. Therefore we are happy to move into the nice suburb of Zahradni ctvrt, since the prices there are lower than in the city."
Erste Bank: "Would it not have been cheaper to rent?"
Barbora Jarosova: "That is not the custom here. Typically, one purchases a property and pays down the mortgage to the bank, in this case, your bank. It's an investment in the future."
Jiri Jaros: "You can see for yourself just how well the country has developed in recent years. Therefore we want to stay here, since we believe that this will continue. I think that this apartment is a good investment."
Erste Bank: "What are your goals for the future?"
Jiri Jaros: "First, we will completely furnish our new house. We have enough room! That will take a while, until we have found everything: furniture, lamps, all the little things that make an apartment comfortable."
Barbora Jarosova: "And at some point we would naturally like to have children. We are planning to try in the next five years. Until then, we will enjoy our new apartment just the two of us. Moreover, in September I just started a new job as an events manager, which I greatly enjoy. I have a lot of responsibility and will be needed there."
Erste Bank: "We wish you a lot of joy in your new apartment and are happy to be able to help you."

Jarosova family, clients of Česká spořitelna, Czech Republic



Net commission income trended very favourably, rising by 37%, or EUR 19.1 million, from EUR 51.7 million to EUR 70.9 million, mainly as a result of higher securities commission income (given the sharp increase in trading volume on the Vienna Stock Exchange) and sales of structured products. The net trading result of EUR 84.5 million was consistent with the previous year level.

General administrative expenses increased by a very slight 0.7%, or EUR 0.6 million, from EUR 93.5 million to EUR 94.1 million thanks to effective cost management. The other operating result improved by EUR 5.8 million from a loss of EUR 7 million to a loss of EUR 1.1 million, mainly as a result of the portfolio's fair value measurement.

CENTRAL EUROPE

Erste Bank's Central Europe segment comprises Erste Bank's operations in the transformation economies of Central and Eastern Europe, covering Česká spořitelna, Slovenská sporiteľňa, Erste Bank Hungary, Erste Bank Croatia and Erste Bank Serbia. While the share purchase agreement for Banca Comerciala Romana was signed on 21 December 2005, BCR will only be consolidated following closing of the transaction.

ČESKÁ SPOŘITELNA

Business profile. Česká spořitelna is the leading retail bank in the Czech Republic and the largest among Erste Bank's operations in Central Europe. Since its privatisation in 2000 the former state savings bank has transformed into a universal bank serving some 5.3 million retail, small and medium enterprise and large corporate clients; it operates a network of 646 branches and over 1,070 ATMs. In addition Česká spořitelna occupies leading positions in fund management, securities trading and foreign exchange dealing.

ECONOMIC REVIEW

In 2005 Česká spořitelna benefited from a strong Czech economy. GDP grew at an estimated 5.0%, the fastest rate in a decade, supported by strong exports, while domestic demand remained subdued, yet positive. GDP/capita reached some EUR 9,600 in 2005, among the highest levels in Central and Eastern Europe. A positive development was also registered in the unemployment rate which stood at 8.3% in 2004 and improved somewhat to about 7.9%.

Inflation remained tame and the Czech Crown continued to appreciate against the Euro both in nominal and real terms. Correspondingly, the Czech National Bank stemmed further upward pressure against its currency by lowering its short term

Key economic indicators – Czech Republic	2002	2003	2004	2005e
Population (ave, million)	10.2	10.2	10.2	10.2
GDP (nominal, EUR billion)	78.4	80.3	86.8	98.2
GDP/capita (in EUR thousand)	7.7	7.9	8.5	9.6
GDP growth (real, in %)	1.5	3.2	4.4	5.0
o/w: domestic demand contribution (in %)	3.4	4.5	2.6	2.3
Exports (% of GDP)	61.5	62.2	71.2	71.9
Imports (% of GDP)	63.6	64.4	71.7	69.7
Unemployment (% of labour force)	7.3	7.8	8.3	7.9
Consumer price inflation (ave, in %)	1.4	-0.1	2.6	1.7
Interest rate (1m interbank offer rate, in %)	3.6	2.3	2.3	2.0
EUR FX rate (ave)	30.8	31.8	31.9	29.8
EUR FX rate (eop)	31.6	32.4	30.5	29.0
Current account balance (% of GDP)	-5.7	-6.3	-5.2	-2.9
General government balance (% of GDP)	-6.8	-12.5	-3.0	-3.2

Source: Eurostat, Czech National Bank.

interest rate to an all-time low of 1.75%. Even though the short term reference rate was raised again towards the end of 2005 to 2%, in line with the European Central Bank's rate actions, Czech rates remained below Euro levels.

The overall positive picture was rounded off by a strongly improving current account balance – once again the trade balance was the chief contributor. The general government balance, while still in negative territory, came in at an estimated 3.2% of GDP, only marginally worse than in 2004, but substantially better than in either 2002 or 2003.

MARKET REVIEW

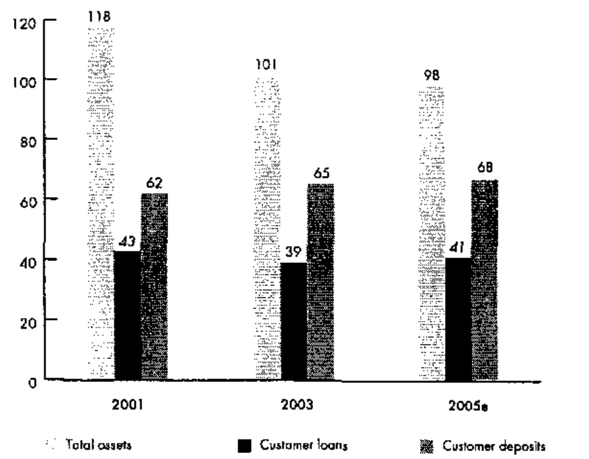
The very favourable economic environment characterised by strong growth, muted inflationary pressures and record low interest rates provided a fertile ground for growth of the Czech banking sector. As a result 2005 was the first year following a severe restructuring process in the late 90-ies and the early years of this decade that saw all benchmark penetration ratios move up.

Total assets/GDP reached 98% in 2005 after years of decline and compared to 95% in 2004. Similarly, customer loan penetration rose to a four year high of 41%, as did deposit penetration which surpassed the 68% mark in 2005. In addition, the general aggregates mask the very positive development in sub segments such as in retail and particularly mortgage lending. Household mortgage lending, for instance, rose from just 1.6% of GDP in 2001 to about 9.3% in 2005. FX lending, which played a dominant role in markets with higher nominal interest rates such as Hungary or Croatia, remained insignificant in the Czech Republic in 2005.

On the back of the positive overall market environment Česká spořitelna once again maintained its No. 1 position in retail banking and continued to rank among the three leading banks in terms of total assets. Its market share of total assets stood at 22% in 2005, unchanged on 2004 and slightly up on 2003.

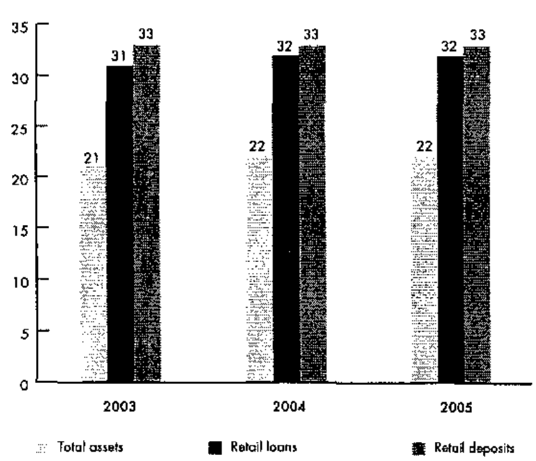
In terms of retail products Česká spořitelna maintained its dominant position owning almost one third of the retail loan and deposit market. In high growth segments of the market, such as residential mortgages, it faired even better, carving out a market share of almost 40%. Česká spořitelna was similarly successful in credit and debit cards, as well as current accounts.

Financial intermediation – Czech Republic (in % of GDP)



Source: Czech National Bank, Eurostat.

Market shares – Czech Republic (in %)



Source: Česká spořitelna, Czech National Bank.

BUSINESS REVIEW

Strategy. Česká spořitelna's strategy remained unchanged in 2005. While maintaining customer satisfaction was an important goal, the continued expansion of its retail lending activities was the main business priority. Through building up a quality loan book, Česká spořitelna aimed to better leverage its large deposit base, leading to a more balanced loan/deposit ratio, which stood at 59% at year-end 2005. The continued shift of excess liquidity into higher margin retail lending products also aimed to support margins and made Česká spořitelna less sensitive to low interest rates.

Strong loan growth. Strong and sustained double-digit loan growth was the major growth driver in 2005. The effects of lower interest rates, compounded by a low, albeit strongly rising loan/deposit ratio were more than compensated by a favourable shift in the asset mix: while the overall loan book posted a healthy gain of 21% year on year, the retail loan book recorded growth in excess of 36%. For the first time in Česká spořitelna's history, total customer loan volume almost reached the EUR 10 billion mark in 2005.

In addition to a very favourable economic environment, loan growth was fuelled by such other factors as improved client advice, product innovation and a generally higher propensity to consume. The latter factor is especially reflected in strong demand for mortgage products and home improvement loans, as well as consumer loans. The dynamic development of loans to small and medium companies and municipalities also contributed to loan growth.

Customer growth in alternative distribution channels. In line with overall business growth Česká spořitelna expanded the number of customers using electronic channels, such as the internet, phone or mobile banking by 13% to above 1 million in 2005. An equally positive trend is the ever larger proportion of clients using credit and payment cards: by the end of 2005 Česká spořitelna had issued some 2.9 million payment cards, while the number of issued credit cards surpassed the 300 thousand mark, translating into exceptional annual growth of 70%.

International and local recognition. As in previous years Česká spořitelna has been awarded a number of local and international awards, first and foremost, for the third year running "The Bank of the Year" award sponsored by "The Banker" magazine. In the local MasterCard Bank of the Year survey, Česká spořitelna regained the title of "Most Trustworthy Bank in the Czech Republic"; it also won four Zlata koruna (Golden Crown) awards for a range of retail banking products, recognising Česká spořitelna's ability to create competitive and high quality retail banking products.

Outlook 2006

In line with its strategic focus Česká spořitelna will continue to grow its retail business, especially on the asset side. Consumer loans, credit cards, mortgages and the financing of small and medium enterprises will dominate the bank's business development efforts in 2006. Česká spořitelna will also continue on the path of headcount reduction, as part of the efficiency programme embarked on in 2005. This is expected to push employee numbers to substantially below 11,000. Financial targets for 2006 are equally ambitious as those for 2005: net profit growth of at least 10%, return on equity in excess of 20% and a cost/income ratio of below 54%. All targets relate to locally reported figures.

Financial review

in EUR million	2005	2004
Pre-tax profit	364.1	289.3
Net profit after taxes and minority interests	265.4	193.7
Cost/income ratio in %	58.6	61.3
Return on equity in %	38.5	39.4

Last year, group net profit increased by 37.1%, or EUR 71.8 million, from EUR 193.7 million to EUR 265.4 million. Aided by the robust earnings growth, the cost/income ratio fell from 61.3% to 58.6%. The return on equity contracted slightly from 39.4% to 38.5%, mainly as a result of the increased equity allocation.

Despite two interest rate cuts by the Czech central bank totalling 50 basis points, net interest income increased by 18.0%, or EUR 90.8 million, from EUR 504.2 million to EUR 595.0 million. This increase was driven mainly by the robust gains in the lending business. The loan loss provision expense increased by EUR 17.9 million from EUR 15.8 million to EUR 33.7 million, mainly as a result of the growth in the lending business.

Starting from its existing high level in 2004, net commission income rose by 9.1% (2.0% adjusted for the currency impact), or EUR 24.1 million, from EUR 262.9 million to EUR 287.0 million. This increase was largely due to the expansion of the payments and asset management businesses as well as the aforementioned gains in the lending business.

Driven by substantial gains in the interest rate derivatives and securities activities, the net trading result also improved consider-ably, rising by 20.5% (12.6% adjusted for the currency impact), or EUR 8.4 million, to EUR 49.4 million.

The 9.9% (2.7% adjusted for the currency impact), or EUR 49.6 million, increase in general administrative expenses from EUR 500.5 million to EUR 550.1 million was mainly due to the establishment of additional severance reserves for the redundancy programme under way and an increase in the sales tax following a tax law change in 2004.

The other operating result increased by EUR 19.5 million from a loss of EUR 10.8 million to a gain of EUR 8.7 million thanks to regulatory changes involving compulsory payments to the deposit insurance fund on the one hand and gains on the disposal of other current assets on the other.

SLOVENSKÁ SPORITEĽŇA

Business profile. Slovenská sporiteľňa is the clear market leader in the Slovakian banking market. The former state savings bank serves some 2.5 million clients, equaling roughly 50% of the Slovak population, through a network of 302 branches. It is the market leader in retail as well as total deposits, and for the first time eclipsed the competition in terms of retail as well as total loans in 2005. In the tailwind of Slovenská sporiteľňa's dominant market position, its asset management subsidiary maintained its No. 1 position, while life insurance provider Poisťovňa SLSP kept gaining market share very fast.

ECONOMIC REVIEW

Slovakia enjoyed another year of stellar economic performance in 2005, thereby supporting Slovenská sporiteľňa in its business development efforts. Real GDP growth amounted to an estimated 5.7%, surpassing last year's 5.5%, and translating into GDP/capita of about EUR 6,900. Growth was supported by FDI-driven gross fixed capital formation and robust private consumption. Within domestic demand, households played an important role reflecting both strong real wage and employment growth – the unemployment rate fell from 18.1% in 2004 to estimated 16.4% in 2005. Strong growth was also reflected in the trade balance, which remained in negative territory on the back of strong import growth.

In 2005 Slovakia made substantial progress in combating inflation: the average rate more than halved to 2.7% from 7.5% in 2004 on the back of a stronger currency and lower regulatory price increases. The upward pressure against the Slovak Crown was also due to an up-tick in foreign direct investment. As a result the Slovak National Bank lowered its short-term reference refinancing rate by another 100 bps to an all time low of 3%.
In line with its all encompassing economic progress, Slovakia entered the Exchange Rate Mechanism II in November 2005, boding well for Euro adoption as early as in January 2009. The resulting reference rate that serves as the mid-point for the 30% fluctuation band was fixed at SKK 38.455.

In 2005 the general government deficit is expected to improve slightly on last year's of 3.1% of GDP, outperforming initial forecasts. At the same time, the current account deficit increased

Key economic indicators – Slovakia	2002	2003	2004	2005e
Population (ave, million)	5.4	5.4	5.4	5.4
GDP (nominal, EUR billion)	25.7	29.0	33.1	37.0
GDP/capita (in EUR thousand)	4.8	5.4	6.2	6.9
GDP growth (real, in %)	4.6	4.5	5.5	5.7
o/w: domestic demand contribution (in %)	4.0	-0.2	2.8	5.3
Exports (% of GDP)	71.7	77.7	76.8	76.8
Imports (% of GDP)	78.9	79.2	79.5	80.8
Unemployment (% of labour force)	18.7	17.5	18.1	16.4
Consumer price inflation (ave, in %)	3.5	8.4	7.5	2.7
Interest rate (1m interbank offer rate, in %)	7.8	6.3	4.8	3.0
EUR FX rate (ave)	42.7	41.5	40.0	38.7
EUR FX rate (eop)	41.5	41.2	38.7	37.8
Current account balance (% of GDP)	-7.3	-0.5	-3.4	-5.4
General government balance (% of GDP)	-7.8	-3.8	-3.1	-3.1

Source: Eurostat, National Bank of Slovakia.

to an estimated 5.4%, on the back of strong domestic demand in 2005, but was covered to a healthy degree by foreign direct investment.

MARKET REVIEW

The strong performance of the Slovak economy created a solid base for the growth of the overall banking market. Low interest rates, combined with growing real wages and higher employment resulted in increased demand for retail loans, particularly mortgages, and also led to shifts on the liability side – clients moved assets from low-yielding deposits into more sophisticated products such as funds and life insurance policies. Hence, after a series of restructuring steps undertaken before 2001, 2005 was the second consecutive year in which all market penetration indicators moved up. This development very much resembles the Czech experience, where 2005 was in fact the first year in which all major market benchmarks improved markedly after a similar clean-up process.

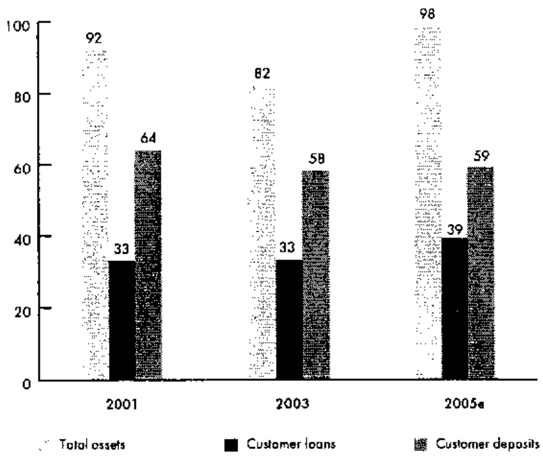
Asset penetration reached a 7-year high of 98%, while loans/GDP moved up to 5-year high of 39%. Deposit penetration remained essentially unchanged on both 2003 and 2004, but down compared to a couple of years ago, on the back of strong household consumption, falling interest rates and an increased uptake of alternative investment products.

Slovenská sporiteľňa once again successfully defended its leading market position in 2005, with a total asset market share of 18.2%. It did especially well in extending its market positions on the asset side. For the first time ever, Slovenská sporiteľňa became the market leader in overall as well as retail lending, reaching market shares of 17% and 25% respectively. It also made significant further inroads into the residential mortgage market by successfully launching asset-backed loans (UverPlus) with real estate as collateral.

BUSINESS REVIEW

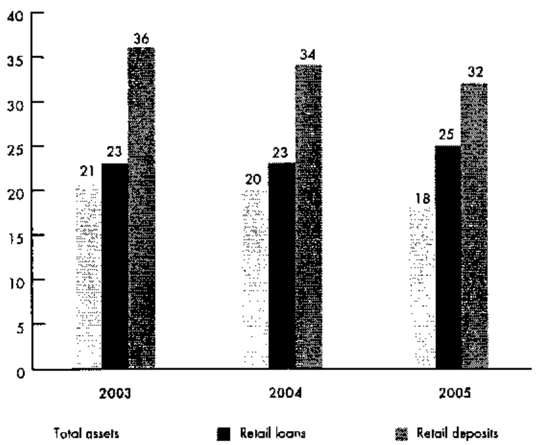
Strategy. The strategic alignment of Slovenská sporiteľňa is very similar to that of Česká spořitelna. While excellent customer service and relevant products remain the key to success for any mass market retail bank, the real issue is an increase in the loan/deposit ratio, which, at 55% has risen strongly on last year's level of 36%, but is the lowest within the entire group. The further improvement of the loan/deposit ratio will support net interest income development in the light of maturing high yielding restructuring bonds in 2006.

Financial intermediation – Slovakia (in % of GDP)



Source: National Bank of Slovakia, Eurostat.

Market shares – Slovakia (in %)



Source: Slovenská sporiteľňa.

Highlights 2005

Above-average loan growth. Vigorous private sector, and in particular household credit expansion was the key business theme of 2005. Growth was supported by a number of innovative product launches, such as so called American mortgages, i.e. home equity loans that allow consumers to extract equity from their property, so called "10 minute" loans that aim to reduce administrative requirements in the loan extension process, and any purpose customer loans. As a result Slovenská sporiteľňa recorded the highest growth rates of any group member, with the overall loan book growing by some 55%, nearly reaching the EUR 2.5 billion mark. Once again, the retail loan book posted the same strong growth of some 54% and accounted for 45% of total customer loans.

Customer growth in alternative channels. Another area in which Slovenská sporiteľňa was doing outstandingly well, is payment transactions. In 2005 more than 90% of customers performed non-cash transactions, used the largest ATM network and made payments with bank cards. We issued almost 38 thousand new bank cards last year, bringing the total number in circulation to nearly 1.1 million. The number of customers using electronic banking has also grown substantially and stood at more than 300 thousand, up by more than 30% as compared with 2004.

Efficiency improvements. After careful analysis, more than 30 inefficient branches were closed down during the course of the year, reducing the number of branches to 302. As a result staff numbers are also fell by some 5% to below 4,800.

Brand awareness and international recognition. Slovenská sporiteľňa was named as the "Best Bank" in Slovakia by The Banker and Euromoney magazines. At the same time, Slovenská sporiteľňa was the best known brand in the Slovak banking market for another year. These results are testament to our strong client orientation continuing improvements in service quality.

100% ownership by Erste Bank. In January, Erste Bank completed the purchase of the remaining 19.99% of the share capital of Slovenská sporiteľňa by exercising the call option

received from the European Bank for Reconstruction and Development and effectively became the 100% owner of the Slovenská sporiteľňa.

Outlook 2006

While Slovenská sporiteľňa expects another strong year in terms of underlying business growth, overall success in terms of profitability will be hampered by the expiry of high-yielding government bonds – volume: EUR 250 million, coupon: 8% – that were received at the time of privatisation in lieu of bad loans and the continued low interest rate environment. All efforts will therefore be directed at increasing customer loans especially in the retail segment, thereby further driving up the loan/deposit ratio. In 2006 Slovenská sporiteľňa aims to keep net profit at last year's level, while further improving its cost/income ratio to below 55% and maintaining its return on equity at 20% (the targets relate to local accounts).

Financial review

in EUR million	2005	2004
Pre-tax profit	100.6	82.6
Net profit after taxes and minority interests	87.3	57.2
Cost/income ratio in %	57.2	59.0
Return on equity in %	47.7	46.1

In 2005, net profit after taxes and minority interests increased by EUR 30.1 million from EUR 57.2 million to EUR 87.3 million. In January, the Erste Bank raised its equity interest in Slovenská sporiteľňa to 100%, with the result that minority interest expenses were no longer incurred and that higher refinancing costs were borne. The return on equity increased from 46.1% to 47.7%, while the cost/income ratio was reduced from 59.0% to 57.2%.

As had been forecast the previous year, the retail business recorded strong gains in 2005. Higher earnings contributions from at equity participations and the favourable currency effect more than offset the aforementioned increase in refinancing costs. Despite the additional burden on the securities portfolio represented by the impact of lower interest rates in Slovakia (redemption of high-yield bonds and adjustment of variable-interest securities to reflect the lower interest rates), net interest income increased by 4.9% (0.9% adjusted for the currency impact), or EUR 9.1 million, from EUR 185.8 million to EUR 194.9 million. Risk provisions rose to EUR 11.1 million, commensurate with the increase in lending volume.

Net provision income rose by 24.2% (19.5% adjusted for the currency impact), or EUR 16.1 million, from EUR 66.4 million to EUR 82.5 million, mainly in the payment transaction, financing and asset management businesses.

General administrative expenses increased by EUR 8.8 million from EUR 158.5 million to EUR 167.3 million. Adjusted for the currency effect, this 1.5% increase was well below the inflation rate.

The EUR 15.2 million improvement in other operating result from a loss of EUR 28.4 million to a loss of EUR 13.2 million can be attributed to proceeds on the sale of fixed-income securities last year as well as non-recurring reserve allocations in 2004.

ERSTE BANK HUNGARY

Business profile. Following the merger with Postabank, Erste Bank Hungary is one of the leading players in Hungarian retail banking. It serves approximately 900 thousand customers through its nationwide network of 160 branches, more than 365 ATMs and about 630 POS terminals. In addition Erste Bank Hungary holds strong and fast growing positions in the area of fund management and leasing.

ECONOMIC REVIEW

In 2005 Erste Bank Hungary benefited from the continued, solid growth of the Hungarian economy. GDP rose by an estimated 4.2%, while GDP/capita reached a level of EUR 8,700. Growth was supported by strong domestic demand, mainly in the form of private consumption and very strong investments. An up-tick in exports also contributed to overall growth. The situation on the labour market was characterised by declining growth in real wages and a concurrent rise in the unemployment rate to 7%, up from 6% in 2004.

Key economic indicators – Hungary	2002	2003	2004	2005e
Population (ave, million)	10.2	10.1	10.1	10.1
GDP (nominal, EUR billion)	69.6	73.5	81.1	88.2
GDP/capita (in EUR thousand)	6.9	7.3	8.0	8.7
GDP growth (real, in %)	3.8	3.4	4.6	4.2
o/w: domestic demand contribution (in %)	8.8	6.1	3.4	3.6
Exports (% of GDP)	64.1	62.7	65.7	66.7
Imports (% of GDP)	66.5	67.2	68.8	69.4
Unemployment (% of labour force)	5.6	5.8	6.0	7.0
Consumer price inflation (ave, in %)	5.2	4.7	6.8	3.6
Interest rate (1m interbank offer rate, in %)	9.2	8.4	11.5	7.2
EUR FX rate (ave)	243.0	253.6	251.7	248.0
EUR FX rate (eop)	236.3	262.5	246.0	252.7
Current account balance (% of GDP)	-7.1	-8.7	-8.8	-8.4
General government balance (% of GDP)	-8.5	-6.5	-5.4	-6.1

Source: Eurostat, Hungarian National Bank.

Annual inflation declined to an estimated 3.6% in 2005. This positive development facilitated a series of interest rate cuts. The Hungarian National Bank lowered its short term reference rate from 9.5% in January 2005 to 6% by the end of the year. Further declines are contingent on the improvement in a number of macro variables, most notably on a reduction of the current account and general government deficits. Persistent weakness in the latter already led to the postponement of the target Euro entry date, allowing more time to meet the criteria of the Stability and Growth Pact. Due to the relatively high level of both nominal and real interest rates, the Hungarian currency remained stable around the HUF 250 mark in 2005.

The Achilles heel of the Hungarian economy is the exuberant attitude towards public spending. This has manifested itself in large general government deficits, which typically become even more pronounced in election years. As 2006 is an election year not much improvement can be expected in this respect, all the more as the VAT rate was slashed to 20% from 25% at the start of 2006.At the same time gross government indebtedness still remains at a much more manageable 58% of GDP, than is the case in many other EU countries. Nonetheless strong government spending has contributed to the external imbalance: the current account deficit again surpassed a level of above 8% to GDP in 2005, but was financed to a healthy degree by foreign direct investments.

MARKET REVIEW

Hungary has benefited from a sound banking sector, sustained market-oriented reforms and large-scale foreign direct investments since the beginning of transition. Accordingly, maturity benchmarks took a much more linear development than either in the Czech Republic or Slovakia. Asset/GDP reached a level of 93% in 2005, up strongly on 68% in 2001. Loan penetration followed a similar trend, rising from 42% in 2001 to 53% in 2005. Over the same period residential mortgage penetration has increased nearly fivefold from 2.2% to 10.4%, and accordingly was the major growth driver underlying credit expansion. Deposit penetration remained essentially unchanged at 45%, reflecting the increased uptake of more sophisticated investment products, such as funds and life insurance policies.

The structure of the Hungarian market differs substantially from that prevailing in our other markets. While the vast majority of banks in terms of assets are privatised and have either strategic or financial owners, the market is dominated by one major player that owns about a quarter of the market in terms assets and up to one third in certain other product categories. A handful of other banks, including Erste Bank Hungary, hold asset market shares in the high single digits, and aim to win market share while maintaining industry profitability.

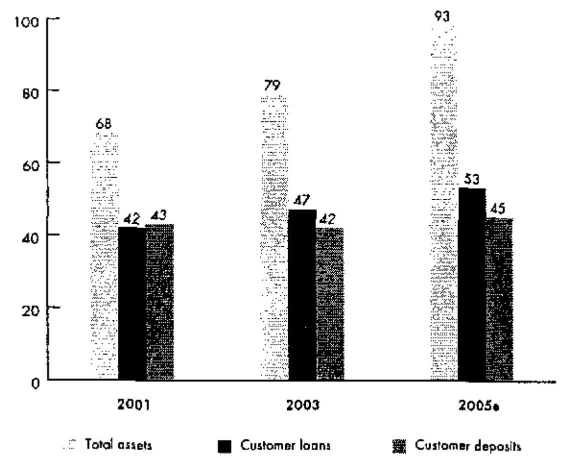
Another peculiarity of the Hungarian banking market that it shares with other markets with high nominal interest rates is the dominance of foreign exchange loans. The vast majority of retail loans in general and mortgages in particular were disbursed in Euros and Swiss Franks in 2005. While this creates a certain level of risk, especially given the potential vulnerability of the Hungarian currency, the downside risk is limited due to prudent loan-to-value ratios, especially in the case of mortgages. Additionally, the Hungarian National Bank has historically managed the currency well, even in the face of high foreign ownership of Hungarian government bonds, as well as external and internal imbalances.

As for Erste Bank Hungary, 2005 was the first year in which it has surpassed the 7% mark in terms of total asset market share. It ranked second by branch numbers and clients. The decline in retail deposit market share has to be viewed in the context of a fourfold increase in fund management market share, which stood at 10.2% at the end of 2005. The strong expansion in retail lending market share to 9.1% is directly related to Erste Bank Hungary's successful focus on the retail market.

BUSINESS REVIEW

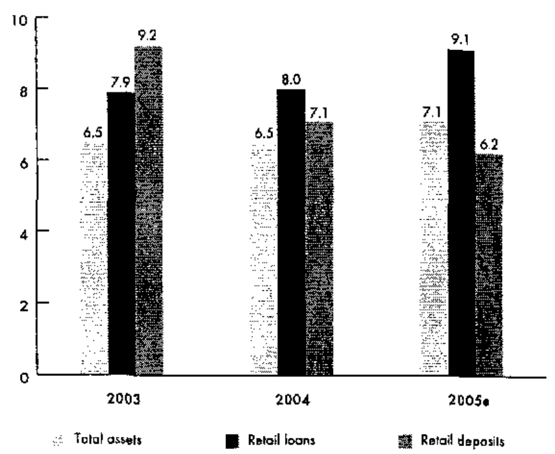
Strategy. The main strategic goal of Erste Bank Hungary – in line with overall group strategy of achieving at least 15 – 20% market share in all markets it operates in – is the expansion of its market position in the Hungarian market. One means by which the bank plans to achieve this is by further deepening its relationship with the Hungarian Post Office: in return for using their outlets as a secondary distribution network, Erste Bank Hungary supplies them with modern banking products ranging from current accounts to bank cards and investment funds. In terms of corporate customers, Erste Bank Hungary focuses on small and

Financial intermediation – Hungary (in % of GDP)



Source: Hungarian National Bank, Eurostat.

Market shares – Hungary (in %)



Source: Erste Bank Hungary, Hungarian National Bank.

medium enterprises which they serve through 25 commercial centres, in addition to mass market retail business.

Highlights 2005

Solid loan growth. As in most other central and east European transformation economies loan growth was the major growth driver within the banking sector. The fastest growing segment within the loan book was retail housing finance. Due to the relatively high level of nominal interest rates in Hungary FX mortgages – mostly denominated in Euro or Swiss Franks – were the product of choice for most customers. Overall, the loan book grew by 27% to a level of nearly EUR 4 billion, while the retail loan book expanded by 41% year on year.

Hungarian Post Office cooperation. The collaboration with the Hungarian Post Office progressed very well in 2005: the number of online postal points reached 248; the partners have developed a completely new technical environment for online working, installed a postal version of the front end used by Erste Bank Hungary; and introduced a web-based user interface for postal employees as well as help desk. All these measures will bear fruit through increased business in future years.

Strength in car leasing. Despite a declining new car market and increased competition, Erste Bank Hungary preserved its No. 4 spot in the Hungarian car leasing market. The key to success were a broader product range, a successfully operating agent network and fully integrated back-office processes.

Outlook 2006

In 2006 Erste Bank Hungary once again targets solid profit growth, an improvement in our cost/income ratio and a return on equity north of 25% (all measures relate to local accounts). The bank will continue to pursue business opportunities in the lower tier SME segment and further develop our relationship with the Hungarian Post Office by establishing an additional 72 online postal points in the first half of 2006 as well as improving mid and back office integration. Erste Bank Hungary will also expand its own branch network to some 200 by the end of 2006. Mortgage and consumer loans will be a continued source of growth.

Financial review

in EUR million	2005	2004
Pre-tax profit	84.3	31.3
Net profit after taxes and minority interests	67.1	31.5
Cost/income ratio in %	61.2	68.1
Return on equity in %	34.1	23.6

All of Erste Bank Hungary's businesses performed well last year. Net profit after taxes and minority interests more than doubled, rising by EUR 35.7 million from EUR 31.5 million to EUR 67.1 million. The cost/income ratio fell from 68.1% to 61.2%, while the return on equity improved from 23.6% to 34.1%.

As expected, the significant expansion of the retail business led to a EUR 30.4 million increase in net interest income from EUR 174.0 million to EUR 204.4 million. Risk provisions totalled EUR 17.1 million, well below the previous year's level, although this figure includes approximately EUR 9 million in releases as a result of the first-time consolidation of Posta Bank.

Net commission income increased by a satisfactory EUR 12.2 million from EUR 52.6 million to EUR 64.8 million, mainly as a result of the gains in the securities and payment transactions businesses.

General administrative expenses rose by a modest 5.8%, or EUR 10.1 million, from EUR 175.7 million to EUR 185.8 million. This increase was largely due to the expansion of the branch network and performance-related compensation.

The sharp rise in the tax expense was due to changes in Hungary's tax law, which calls for a special 8% tax on financial institutions and leasing companies.

ERSTE BANK CROATIA

Business profile. Erste Bank Croatia is one of the largest and fastest growing universal banks in Croatia, serving about 600 thousand clients through a nationwide network of 122 branches. While its core strength is retail banking, it is also the market leader in treasury products, such as in fixed income, foreign exchange and derivatives trading, as well as in fund management. In addition, Erste Bank Croatia successfully distributes a wide range of para-banking products in the areas of asset management, life insurance, securities brokerage, leasing and pension funds.

ECONOMIC REVIEW

In 2005 Erste Bank Croatia benefited from continued stable growth of the Croatian economy. GDP grew by an estimated 3.6% in 2005, while GDP/capita reached a level of some EUR 6,700. Strong domestic demand in the form of private consumption and public investments was the major growth driver. Exports did not contribute significantly to overall growth, but still played an important role through the generation of substantial tourism revenues. The unemployment rate improved slightly to an estimated 13.3% in 2005, down from 13.8% in the previous year.

Annual inflation remained relatively low at 3% in 2005. Nevertheless, this meant a full percentage point increase on the level of 2004, mainly due to higher energy and food prices as well as higher excise taxes. The Croatian National Bank remained committed to exchange rate stability in 2005, mainly through the maintenance of relatively high nominal and real interest rates – the discount rate stood at a level of 4.5% for the third consecutive year. As a result the Croatian currency, the Kuna, remained unchanged against the Euro.

On the fiscal side, the general government deficit improved to an estimated 4.5% of GDP in 2005, a slight improvement on the previous year, but substantially up on 2003. A continuation of this trend is dependent on additional reforms of the pension and health care systems. The current account deficit expanded from 5.3% to 6.2%, on the back of stronger public spending, even though the trade balance improved year-on year.

MARKET REVIEW

The Croatian banking system ranks among the most developed in terms of banking intermediation levels. Its continued growth was supported by a stable economic environment. The asset/GDP ratio stood at 116% in 2005, up strongly from 86% recor-

Key economic indicators – Croatia	2002	2003	2004	2005e
Population (ave, million)	4.4	4.4	4.4	4.4
GDP (nominal, EUR billion)	24.2	25.5	27.6	29.7
GDP/capita (in EUR thousand)	5.4	5.7	6.2	6.7
GDP growth (real, in %)	5.2	4.3	3.8	3.6
o/w: domestic demand contribution (in %)	6.8	6.5	3.5	3.4
Exports (% of GDP)	45.4	47.1	47.5	48.9
Imports (% of GDP)	54.7	56.8	55.7	56.4
Unemployment (% of labour force)	14.7	14.1	13.8	13.3
Consumer price inflation (ave, in %)	1.7	1.8	2.1	3.0
Interest rate (1m interbank offer rate, in %)	3.6	5.3	7.0	6.0
EUR FX rate (ave)	7.4	7.6	7.5	7.4
EUR FX rate (eop)	7.5	7.6	7.7	7.4
Current account balance (% of GDP)	-8.6	-7.4	-5.3	-6.2
General government balance (% of GDP)	-5.0	-6.3	-4.9	-4.5

Source: Eurostat, European Commission.